

Should Article 3 of the Uniform Commercial Code Be Adopted in Ohio?

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INTRODUCTION

Article 3 of the Uniform Commercial Code deals with commercial paper.¹ The Negotiable Instruments Law was written in 1896 and adopted in Ohio in 1902, and consequently there has been a long period in which to discover the defects or "bugs" in that Law. Article 3 of the new Code is concerned with an attempted elimination of those "bugs."

In many respects the language of the Negotiable Instruments Law has proved ambiguous. Professor Beutel, an authority on the subject, has stated that in at least 70 sections of the Law the courts have differed in their interpretations. Moreover, in the 50-odd years of operation under the Negotiable Instruments Law, new commercial customs have developed which render parts of the old Law obsolete.

Thus, the chief purposes of Article 3 of the new Code are to clarify the existing law, to settle conflicts in the interpretation of the Negotiable Instruments Law, and to give legislative recognition to current customs.

In this paper no attempt will be made to cover every detail of the new Code and its Comments, nor to engage in analytical discussion of the various problems, nor to attribute to the drafters of the Code some deep-rooted philosophy or approach which in reality did not exist. After all, they approached their task problem by problem, and I will reflect their approach in this article and will merely call attention to a number of the more significant provisions and endeavor to indicate briefly the purposes of the Code and, where necessary, how it changes the present law.

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¹ Among periodical literature pertaining to Article 3 are the following: Beutel, *Comparison of the Proposed Commercial Code, Article 3, and the Negotiable Instruments Law*, 30 NEB. L. REV. 531 (1951) (disapproving adoption of the Uniform Commercial Code, Article 3); Cosway, *Innovations in Articles Three and Four of the Uniform Commercial Code*, 16 LAW & CONTEMP. PROB. 284 (1951); Emblidge, *Commercial Paper Under the Proposed Uniform Code*, 23 N. Y. STATE BAR ASS'N BULL. 371 (1951); Leary, *Some Clarifications in the Law of Commercial Paper Under the Proposed Uniform Commercial Code*, 97 U. OF PA. L. REV. 354 (1949); Palmer, *Negotiable Instruments Under the Uniform Commercial Code*, 48 MICH. L. REV. 255 (1950); Sutherland, *Article 3—Logic, Experience and Negotiable Paper*, [1952] WIS. L. REV. 230.

Although Ohio cases will be cited, I will not encumber the article by too many citations. In the absence of citation, it may be assumed that there is no serious obstacle, decision-wise, to the adoption of the specific code section.

For the sake of brevity I will use the abbreviations NIL and UCC for the Negotiable Instruments Law and the Uniform Commercial Code, respectively.

An important feature of the UCC, which runs through the whole Code, is Section 1-102 (3) (f), providing that the Comments may be consulted in the construction and application of the Code. From that source is derived a mine of material disclosing the intention of the codifiers. If the Code is adopted, some means must be found for making the Comments available to lawyers and judges.

PART I.

SHORT TITLE, FORM AND INTERPRETATION.

Section 3-102 (1) (c) clarifies a somewhat troublesome situation. It provides: "A 'promise' is an undertaking to pay and must be more than an acknowledgement of an obligation." Under Section 1(2) of the NIL,² an instrument, to be negotiable, must contain an unconditional promise to pay a sum certain in money. Confusion has arisen in the case of instruments acknowledging debts but not containing words promising to pay. Other variations of language have likewise caused difficulty. For example, in *Shemonia v Verda*³ the instrument read, in substance: "I borrow money from [plaintiff], the sum of \$500 with 4% interest. The borrowed money ought to be paid within four months from the above date." Although the issue was whether the paper constituted an instrument for the unconditional payment of money, within the statute authorizing a short form of pleading,⁴ the court went beyond the bare necessities of the case and held that the instrument was a promissory note. However, the court added that Section 11334 of the Ohio General Code comprehends instruments which do not contain all the elements of a promissory note.

The Comment to the UCC subsection cited above recites the exact wording of the instrument in the *Shemonia* case and states that the subsection is intended to change the holding therein so far as the promissory note element is concerned. In view of the infrequency of such strange instruments, and the more logical approach of the UCC, the change is completely justified. The subsection also makes it clear that an "I.O.U.," containing no promissory language, is not a promissory note. The same is true of an instrument reading, "Due John Smith \$100."

² OHIO GEN. CODE Sec. 8106 (2).

³ 24 Ohio App. 246, 157 N.E. 717 (1927).

⁴ OHIO GEN. CODE Sec. 11334.

Section 3-103 (1) represents one of the most significant developments in the UCC. By Section 1 of the NIL,⁵ an instrument, to be negotiable, must conform to certain requirements, including, for example, the requirement that it be payable in money. But in the years since 1896, when the NIL was written, the business world has created new instruments, treated by businessmen as negotiable, yet sometimes lacking some element required by the NIL. An example is the interim certificate, in which the promise is not to pay in money but is to deliver definitive bonds. Faced with the language of the NIL, courts have held that such nonconforming instruments are not negotiable. Thus, the law is at odds with business custom and prevents the development of new categories of negotiable instruments.

The UCC cures the evil by the subsection referred to, which states that Article 3 "does not apply to . . . investment securities." Such instruments are covered in Article 8, which recognizes the needs of business in this respect.

It is interesting to observe that an Ohio court has reached the desirable result in an interim certificate case — partly by holding that the NIL is not intended to cover interim certificates and that the law merchant must be left free to develop new instruments, unhampered by the NIL.⁶

Subsection (2) subjects Article 3 to the provisions of Article 4, entitled "Bank Deposits and Collections," and Article 9, dealing with secured transactions, including chattel paper. Other papers in this series will deal with Articles 4 and 9; consequently, they will not be discussed here.⁷

Section 3-104 (2) defines the instruments included in Article 3. These consist of drafts, checks, certificates of deposit, and notes. The subsection brings into one place, definitions which are widely scattered in the NIL. It should be noted that the UCC prefers the word "draft" to the term "bill of exchange."

Section 3-105 is both important and comprehensive. It arises from difficulties in connection with NIL Section 3,⁸ stating that an order or promise is unconditional, though coupled with certain things, including indication of a particular fund or account and a statement of the transaction which gives rise to the instrument. The NIL then states that an order or promise to pay out of a particular

⁵ OHIO GEN. CODE Sec. 8106.

⁶ *Hopple v. Cleveland Discount Co.*, 25 Ohio App. 138, 157 N.E. 414 (1927).

⁷ See Sutherland, *Article 3—Logic, Experience and Negotiable Paper*, [1952] WIS L. REV. 230, 235, for a discussion of the "consumer goods" provisions of Article 9. These provisions relate to the position of the purchaser of "chattel paper."

⁸ OHIO GEN. CODE Sec. 8108.

fund is not unconditional. It is obvious that the NIL is rather general and leaves some situations in the air.

Without enumerating all the problems solved by this section of the UCC, I will mention some important ones and show how the UCC handles them.

1. The instrument contains a recital of the consideration for which it was issued. The recital shows that the consideration is executory. Although the majority rule upholds negotiability, some courts hold that payment is conditioned upon performance by the payee and therefore the promise to pay is conditional.⁹ This view overlooks the fact that the NIL attempts to distinguish between express and implied conditions. The latter are no part of the instrument; therefore the promise is unconditional and a holder in due course may recover despite the failure of the payee to perform.

Two Ohio cases, decided in the same appellate district fifteen years apart, take opposite views on the problem.¹⁰ However, in the earlier case a payee is suing, and perhaps this may serve as a distinguishing factor, although the contrary conclusions of the two courts are based upon opposite viewpoints toward the problem at hand. Subsections (1) (a) and (1) (b) of Section 3-105 of the UCC provide that a promise or order otherwise unconditional is not made conditional by the recital in question, thus being in accord with the more recent of the Ohio decisions.

2. A conflict of authority has arisen in connection with instruments reciting that they are made "in accordance with" or "as per" a contract of even date, etc.¹¹ Section 3-105(1) (b) upholds their negotiability. This represents the more realistic view, and there is nothing to indicate that Ohio is *contra* at the present time.

3. A similar problem arises with the trade acceptance which recites: "The obligation of the acceptor arises out of the purchase of goods from the drawer, maturity being in conformity with the original terms of purchase." The majority rule is that the last clause renders the promise conditional—again an unrealistic

⁹ BRITTON, *BILLS AND NOTES* Sec. 16 (1943). This book will be cited as BRITTON, followed by the section or page and omitting the date of publication.

¹⁰ *Haley v. King*, 3 Ohio App. 323, 21 Ohio Cir. Ct. (N.S.) 364, 26 Ohio Cir. Dec. 259 (1914) (holding that the instrument was not a promissory note); *Cincinnati Brush & Mop Mfg. Co. v. Weber*, 35 Ohio App. 506, 172 N.E. 568 (1929) (negotiable note). The opinion in the second case makes no reference to the first.

¹¹ BRITTON 52. Professor Britton states the correct rule that the "as per" recital does not render the promise conditional, but there are cases *contra*, e.g., *Continental Bank & Trust Co. v. Times Publishing Co.*, 142 La. 209, 76 So. 612 (1917). See Notes, 14 A.L.R. 1126 (1921); 33 A.L.R. 1173 (1924); 37 A.L.R. 655 (1925); 61 A.L.R. 815 (1929); 104 A.L.R. 1378 (1936).

view.¹² In Subsections (1) (b) and (1) (c) the UCC adopts the minority rule. Ohio has reached the result of the minority rule on the ground that although the words incorporate the trade acceptance, the incorporation relates to maturity only and does not affect the absolute promise to pay.¹³

4. The instrument states that it is for the sale of certain personal property and that title to the property shall remain in the seller until the instrument has been paid. It is difficult to see how such a recital renders the promise to pay conditional, but some courts so hold.¹⁴ Subsection (1) (e) adopts the correct rule that the recital does not make the promise conditional.

5. In accordance with the NIL, the UCC, in Subsections (2) (a) and (b) of Section 3-105, makes the promise conditional if it is subject to or governed by another agreement or, generally, if it is to be paid only out of a particular fund. However, under Subsection (1) (g), if the instrument is issued by a government or governmental agency or unit, payment may be limited to a particular fund. This accords with the practicalities of the situation.

Section 3-106 deals with sum certain. NIL Sections 1 and 2¹⁵ contain the corresponding provisions under present law. The UCC adds a new provision, Subsection (1) (c), providing that the sum is certain even though it is to be paid with a stated discount if paid before the date fixed for payment. The NIL is silent on the point, and the majority view seems to be against negotiability.¹⁶ Ohio has not passed upon the point.

Section 3-107, defining "money," performs a useful service by stating rules applicable to instruments drawn payable in a foreign currency. To put the matter mildly, the cases are confusing¹⁷ and clarification is sorely needed.

Section 3-109 contains provisions of importance.

In the first place, in conjunction with Section 3-104(1) (c), it excludes instruments payable at a "determinable future time." Such instruments are recognized by NIL Sections 1(3) and 4(3),¹⁸ and include those made payable at or after the death of a named person. In reality there is no certain time of payment for this sort of instrument, because it is payable at or after the happening of an

¹² *E.g.*, *Westlake Mercantile Finance Corp. v. Merritt*, 204 Cal. 673, 269 Pac. 620 (1928). *Contra*: *Heller v. Cuddy*, 172 Minn. 126, 214 N.W. 924 (1927).

¹³ *State Trade Corp. v. Tobias Studio*, 64 Ohio App. 516, 29 N.E. 2d 38 (1940).

¹⁴ BRITTON Sec. 14.

¹⁵ OHIO GEN. CODE Secs. 8106, 8107.

¹⁶ *E.g.*, *Waterhouse v. Chouinard*, 128 Me. 505, 149 Atl. 21 (1930). It must be admitted that such a note is mathematically uncertain as to sum.

¹⁷ BRITTON 126.

¹⁸ OHIO GEN. CODE Secs. 8106 (3), 8109 (3)

event the time of the happening of which is uncertain, even though the event itself is certain to occur. Inquiry among bankers has elicited the fact that the commercial world does not regard such a note as negotiable, and the UCC thus rids us of a useless appendage.

A second important change involves acceleration clauses. NIL Section 4 (2)¹⁹ is too indefinite, and, in general, courts have followed their own common law. The majority rule is that if the holder has an uncontrolled option to accelerate the due date, the instrument is uncertain as to time and, therefore, not negotiable.²⁰ This rule overlooks the actualities of the situation, for such an acceleration clause makes the instrument more negotiable in fact. The UCC change is beneficial.

The NIL gives no help in determining the effect of an extension clause on negotiability. Section 3-109 (1) (d) fills the gap effectively.

Section 3-110, explaining when an instrument is and is not payable to order, clarifies and, to some extent, changes existing law. Section 8 is the corresponding part of the NIL.²¹

In Subsection (1) the UCC section makes an instrument payable to the assigns of a specified person negotiable, assuming, of course, that it complies in all other respects.

In Subsection (1) (e) it includes within the order instrument category, instruments payable to an estate, trust, or fund. There are decisions under the NIL holding that such instruments are bearer paper because the name of the payee does not purport to be the name of any person.²² This overlooks the intent of the maker.

Under Section 8 (6) of the NIL, dealing with instruments payable to the holder of an office for the time being, there has been some difficulty.²³ Section 3-110 (1) (f) of the UCC straightens out the trouble by providing that an instrument payable to an office or officer as such is payable to the order of the incumbent of the office or his successors.

Subsection (1) (g) provides for instruments payable to the order of a partnership or unincorporated association, and states that such an instrument may be indorsed or transferred by any person thereto authorized. The provision frees us from the concept that the payee must be a legal entity and that otherwise the paper is bearer rather than order. The NIL is silent on the point.

Subsection (2) provides that such words as "payable upon

¹⁹ OHIO GEN. CODE Sec. 8109 (2).

²⁰ BRITTON Sec. 28.

²¹ OHIO GEN. CODE Sec. 8113.

²² *E.g.*, *Hansen v. Northwestern National Bank*, 175 Minn. 453, 221 N.W. 873 (1928).

²³ BRITTON Sec. 46.

return of this instrument properly indorsed" do not of themselves make the instrument payable to order, and such an instrument is thus nonnegotiable. This differs from the majority rule under the NIL²⁴ and from the pronouncement of an Ohio court.²⁵ Most, if not all of the cases concern certificates of deposit. The UCC provision is based upon the logical assumption that by omitting the word "order" in the certificate, the bank intends to make the certificate nonnegotiable. This position is strengthened by a survey made some years ago which revealed that practically all banks included "to the order of" in their certificates of deposit.²⁶

Section 3-112, enumerating terms and omissions not affecting negotiability, contains an important provision in Subsection (1) (c), which states that the negotiability of an instrument is not affected by a promise to give additional collateral on demand. Section 5 of the NIL²⁷ provides that an instrument which contains an order or promise to do any act in addition to the payment of money is not negotiable. Literally, that would include a promise to give additional collateral, and many courts have so held.²⁸ But such a decision fails to recognize the purpose of the section, which was never intended to take away negotiability because of a promise to bolster the security. The UCC change is a distinct improvement.

Section 3-115 (2), dealing with incomplete instruments, changes the law for the better in one important respect. The subsection must be considered with Sections 3-305 and 3-407. Section 15 of the NIL²⁹ states that where an incomplete instrument has not been delivered it will not, if completed and negotiated without authority, be a valid contract in the hands of any holder as against any person whose signature was placed thereon before delivery. This means that even a holder in due course loses, which seems unfair. Should not the loss fall upon the person who made the fraud possible by signing blank paper? Some courts place the loss upon the maker if he has been negligent, thus making an exception to the strict terms of the statute.³⁰ The UCC sections referred to place the holder in due course in the preferred position and allow him to recover.

Section 3-119 is new and attempts to set forth the rules relating to a negotiable instrument issued contemporaneously with another document, such as a mortgage. The problem has caused

²⁴ BRITTON 37.

²⁵ *Felton v. Commercial National Bank*, 39 Ohio App. 24, 177 N.E. 52 (1930).

²⁶ 20 COL. L. REV. 621 (1920).

²⁷ OHIO GEN. CODE Sec. 8110.

²⁸ BRITTON Sec. 36.

²⁹ OHIO GEN. CODE Sec. 8120.

³⁰ BRITTON Sec. 88.

difficulty among the courts. The UCC makes it clear that the separate agreement does not affect negotiability, unless, as we noted in discussing Section 3-105, words in the instrument expressly incorporate the separate agreement. The present section also explains the effect upon a holder of the two instruments of limitations in the separate agreement.

Section 3-121, relating to instruments payable at a bank, is mentioned here because it provides alternatives, depending upon local commercial and banking practice. The note is made payable at a particular bank and the question is whether or not it is to be regarded as the equivalent of a draft drawn on the bank payable out of funds of the maker in account with the bank. The alternative is that the note is not an order to the bank to pay it. Before recommending an alternative, the proponents of the UCC in Ohio should be informed of the Ohio practice. The New York practice treats it as a draft.

PART II.

TRANSFER AND NEGOTIATION.

As its title implies, this part deals with the transfer of negotiable instruments and includes the several kinds of indorsement. Certain features deserve comment.

The first appears in Section 3-201(1) and affects a transferee from a holder in due course. Section 58 of the NIL³¹ puts a holder who derives his title through a holder in due course in the shoes of the latter provided the transferee is not himself a party to any fraud or illegality affecting the instrument. This leaves open the case of a person who is not a party to any fraud but who as a prior holder had notice of a defense, transferred the instrument to a holder in due course, and reacquired it. The section prohibits him from improving his prior position by this dodge.

Section 3-202(4) contains an important provision not found in the NIL. Examples will indicate the problems.

1. John Smith is the payee. He transfers the note to Henry Jones, writing on the back of it, above his signature, the words, "I assign all my right, title and interest in the within note to Henry Jones."

Is this an indorsement or an assignment? Practically every state now holds that it is an indorsement.³² Smith is using the words to transfer whatever he can, and it is foolish to say that he is trying to give less than the law allows and to prevent Jones from becoming a holder in due course. Nevertheless, a Court of Appeals in Ohio has held it a mere assignment.³³ And a United States District

³¹ OHIO GEN. CODE Sec. 8163.

³² BRITTON Sec. 58.

³³ *Carius v. Ohio Contract Purchase Co.*, 30 Ohio App. 57, 164 N.E. 234 (1928).

Court has recognized that case as the law in Ohio.³⁴ The UCC will overthrow the case and place Ohio in the proper column. The subsection states that words of assignment accompanying an indorsement do not affect its character as an indorsement.

2. Smith writes above his signature the words "I guarantee payment." Although many courts hold that this is an indorsement so far as negotiating the instrument is concerned, there are decisions *contra*.³⁵ The subsection of the UCC includes these words along with the words of assignment. Consequently the transfer to Jones is a negotiation and makes him a holder. The effect of the words on Smith's liability is covered in Section 3-416.

Section 3-204. *Special Indorsement; Blank Indorsement*. Another problem, which by reason of the paucity of cases combined with its intriguing nature has caused more concern to the teachers and writers than to the courts, is solved by the above section, which, in part at least changes the law. As a result of the section, a bearer instrument or an order instrument indorsed in blank is negotiable by delivery, as at present, but only until someone indorses it specifically, after which it may not be further negotiated without indorsement. The various sections of the NIL here involved will be found in the UCC Comments. The one clearly repealed is section 40.³⁶ The change is an improvement.

Section 3-206. *Indorsement "For Collection," "For Deposit," to Agent or in Trust*. This section dispenses with the term "restrictive indorsement," found in NIL Sections 36 and 37.³⁷ As employed in the NIL, the term is used too broadly, as a result of which confusion and injustice have arisen. For example, the sections practically compel a holding that neither a restrictive indorsee nor his transferee may become a holder in due course even if he gives value. Moreover, they are so worded as to bring about this result even in the case of a trustee who buys the instrument for value.

PART III.

RIGHTS OF A HOLDER.

Section 3-302 sets forth certain requirements necessary to constitute one a holder in due course and specifies certain instances where one does not become a holder in due course.

In requiring good faith, Subsection (1) (b) includes observance of the reasonable commercial standards of any business in which

³⁴ United States v. Hill, 57 F. Supp. 934 (N.D. Ohio 1944).

³⁵ BRITTON Sec. 59.

³⁶ OHIO GEN. CODE Sec. 8145.

³⁷ OHIO GEN. CODE Secs. 8141, 8142.

the holder may be engaged.³⁸ A businessman should not receive the benefit of the holder in due course status unless his actions meet such standards.

Subsection (1) (c) remedies a defect in Section 52 (2) of the NIL,³⁹ requiring the holder to take the instrument before it is overdue, in order to become a holder in due course. As usually construed, the NIL prevents a completely innocent holder of an instalment note from becoming a holder in due course after a default in one or more instalments.⁴⁰ It is true that the overdue feature is often intermingled with the question of notice of dishonor, but together they bring about the undesirable result even though the purchaser does not know of the dishonor or nonpayment. An Ohio Court of Appeals case so holds.⁴¹ The UCC changes the result by making *notice* that the instalment is overdue the test. So far as dishonor is concerned, notice is required in both codes. This section must be read with Section 3-304 (4) (a).

Subsection (2) permits a payee to be a holder in due course. Largely by reason of the word "negotiated" in NIL Section 52 (4),⁴² some courts have held that the payee may never be a holder in due course. This is contrary to the majority view at common law.⁴³ A federal court in Ohio has said that the exact point has not been settled in Ohio.⁴⁴

Section 3-303. *Taking for Value*. Subsection (a) solves an apparent conflict between NIL Sections 25 and 54.⁴⁵ Section 25 states that value is any consideration sufficient to support a simple contract. Is crediting an account value? There are cases both ways.⁴⁶ But Section 54 states that where the transferee receives notice of an infirmity or defect before he has paid the full amount agreed to be paid, he will be deemed a holder in due course only to the extent of the amount theretofore paid by him. This indicates that mere crediting is not enough. The UCC takes the latter position, specifying that a holder takes the instrument for value to the extent that the agreed consideration has been performed.

Section 3-303 (c) solves another puzzle by providing that a holder takes an instrument for value when he gives a negotiable instrument for it.

³⁸ The UCC Comment to Section 3-302 states that the "reasonable commercial standards" language makes explicit what has long been implicit in case-law handling of the good faith concept.

³⁹ OHIO GEN. CODE Sec. 8157.

⁴⁰ BRITTON 455.

⁴¹ Harvard Mortgage Co. v. Neeson, 6 Ohio L. Abs. 577 (1928).

⁴² OHIO GEN. CODE Sec. 8157 (4).

⁴³ BRITTON Sec. 122.

⁴⁴ United States v. Hill, 57 F. Supp. 934 (N.D. Ohio 1944).

⁴⁵ OHIO GEN. CODE Secs. 8130, 8159.

⁴⁶ BRITTON Sec. 97.

Section 3-304. *Notice to Purchaser.* This is one of the most important sections in the UCC. Sections 52, 55, and 56 of the NIL,⁴⁷ dealing with good faith and notice, do not attempt to spell out what is and what is not notice. The UCC, on the other hand, specifically covers a number of rather common situations, many of which have led to uncertainty and conflict in the present law. Some of these will now be mentioned.

Subsection (1) (a) refers, among other things, to incomplete instruments. NIL Section 52 (1)⁴⁸ requires that a person, in order to be a holder in due course, must take an instrument complete on its face. Inasmuch as a person who is not a holder in due course is subject to defenses under NIL Section 58,⁴⁹ one who purchases an incomplete instrument finds himself in an unenviable position, no matter how innocent he may be and even though, pursuant to NIL Section 14,⁵⁰ he fills up the instrument in accordance with the actual authority given by the maker to the payee.⁵¹ The same result is reached where he takes a complete instrument but knows that it was originally incomplete when issued.⁵²

Sections 3-304(1) (a) and (5) (d) are evidently intended to change the rule. The latter subsection provides that the purchaser is not given notice of a defense or claim by reason of his knowledge that an incomplete instrument has been completed, unless he has knowledge of an improper completion. The Comment says, "It is intended to mean that the holder may take in due course even though a blank is filled in his presence, if he is without notice that the filling is improper."

Subsection (2) (b) provides that the purchaser has notice of a claim against the instrument when he has reasonable grounds to believe that a fiduciary has negotiated the instrument in payment of or as security for his own debt or in any transaction for his own benefit or otherwise in breach of duty. The counterpart is Subsection (5) (e), stating that knowledge that any person negotiating the instrument is a fiduciary does not of itself give the purchaser notice of a defense or claim. Conflicts in the common law rules have been resolved by the Uniform Fiduciaries Act, adopted in Ohio in 1943.⁵³ The UCC is consistent with that Act in this respect. Consequently, there will be no change in Ohio law.

Subsection 4(a) is so important that I will mention it again

⁴⁷ OHIO GEN. CODE SECS. 8157, 8160, 8161.

⁴⁸ OHIO GEN. CODE SEC. 8157 (1).

⁴⁹ OHIO GEN. CODE SEC. 8163.

⁵⁰ OHIO GEN. CODE SEC. 8119.

⁵¹ *But cf.* First Discount Corp. v. Hatcher Auto Sales, Inc., 156 Ohio St. 191, 102 N.E. 2d 4 (1951).

⁵² BRITTON 471.

⁵³ OHIO GEN. CODE SECS. 8509-7-8509-19, *sub nom.* Uniform Fiduciary Act.

even though I discussed it in part under Section 3-302(1) (c), which complements it. Those sections result in a holder in due course status for the purchaser of a note payable in instalments unless he has reasonable grounds to believe that any part of the principal is overdue or that there is an uncured default in payment of another instrument of the same series.

Subsection 4(b) resolves properly another difficult problem. It refers to acceleration and deals with the following situation. A note containing an acceleration clause is actually accelerated and thereby becomes due. It is then negotiated to Smith, who knows nothing of the acceleration. Since technically he takes after maturity, he is not a holder in due course under NIL 52.⁵⁴ He should be a holder in due course and he attains that status under the present subsection and Section 3-302(1) (c), which make the test reasonable grounds to believe that acceleration has been made.

Subsection (4) (c) helps to clarify the law in an important respect. Section 53 of the NIL⁵⁵ provides that where an instrument payable on demand is negotiated an unreasonable length of time after its issue, the holder is not deemed a holder in due course. With reference to checks, the UCC gives us a yardstick by creating a thirty-day presumption of reasonable time.

Subsection (5) (b) settles two points upon which the decisions are in conflict. First it provides that knowledge that the instrument was issued or negotiated in return for an executory promise does not of itself give notice of a defense or claim.⁵⁶ Secondly, it provides that mere knowledge that the instrument was accompanied by a separate agreement does not of itself give the purchaser notice of a defense or claim, and thus he takes in good faith unless otherwise he has notice that a defense or claim has arisen from the terms thereof. This is obviously the just rule.⁵⁷

Finally, Subsection (5) (f) settles another conflict by providing that knowledge of a default in the payment of interest does not constitute notice of a defense or claim.⁵⁸

Section 3-305(2) frees the holder in due course from certain defenses. However, in Subsection (c) it recognizes fraud in the factum as a real defense unless the signer had a reasonable opportunity to obtain knowledge of the character of the instrument or its essential terms. Fraud in the factum relates to fraud whereby the signer thinks he is signing some other kind of document. Even un-

⁵⁴ OHIO GEN. CODE Sec. 8157. Cf. *Union Central Bank v. Hall*, 14 Ohio L. Abs. 420 (Ct. of App. 1933).

⁵⁵ OHIO GEN. CODE Sec. 8158.

⁵⁶ See BRITTON Sec. 108; *accord*, *Motor Finance Corp. v. Huntsberger*, 116 Ohio St. 317, 156 N.E. 111 (1927).

⁵⁷ But see *supra* note 7 about chattel paper.

⁵⁸ See BRITTON Sec. 110.

der the NIL, most courts hold fraud in the factum a real defense and thus not cut off in the hands of a holder in due course in the absence of negligence on the part of the maker.⁵⁹

Section 3-306(a) provides that unless he has the rights of a holder in due course any person takes the instrument subject to all valid claims to it on the part of any person. Some courts have held that an innocent holder for value who takes after maturity and therefore is not a holder in due course will be preferred as against a person having an equitable right to the instrument.⁶⁰ The theory is that this does not concern liability on the instrument but rather ownership of the instrument or its proceeds, for which reason the NIL is inapplicable. Other courts hold *contra*.⁶¹ The position of the UCC is with the latter, and Ohio is in accord.⁶²

Section 3-307(3) settles a point not clear under NIL Section 59.⁶³ Although, of course, a holder, whether in due course or not, may recover where there are no defenses, if there is a defense he has the burden of proof as to the elements necessary to constitute him a holder in due course.⁶⁴ The UCC uses the term "burden of establishing," which is defined in Section 1-201(8). There are several Ohio cases in agreement with the UCC,⁶⁵ although the Ohio law was different before the NIL.⁶⁶

PART IV.

LIABILITY OF PARTIES.

Considerable improvement, simplification, and clarification have been effected in Part IV.

Section 3-403(2). *Signature by Authorized Representative*. This section, combined with Section 1-201(35), defining "representative" makes it clear that officers of unincorporated associations, trustees, executors, administrators, and the like, may sign in a *representative capacity* despite the fact that the thing they represent is not technically a legal entity.

The section also prohibits parol evidence to show whether or not the person signed in a representative capacity. It provides that an authorized person who signs his own name to an instrument is

⁵⁹ *Gross v. Ohio Savings & Trust Co.*, 116 Ohio St. 230, 156 N.E. 205 (1927); *BRITTON* Sec. 130.

⁶⁰ *E.g.*, *Justice v. Stonecipher*, 267 Ill. 448, 108 N.E. 722 (1915).

⁶¹ *BRITTON* Sec. 156.

⁶² *Osborn v. McClelland*, 43 Ohio St. 284, 1 N.E. 644 (1885) (before the NIL); *Uhl v. First Nat. Bank*, 120 Ohio St. 356, 166 N.E. 213 (1929).

⁶³ OHIO GEN. CODE Sec. 8164.

⁶⁴ See *BRITTON* Sec. 104 as to the situation under the NIL.

⁶⁵ *E.g.*, *Kuchenbacher v. Gill*, 18 Ohio Cir. Ct. (N.S.) 535, 33 Ohio Cir. Dec. 192 (1911).

⁶⁶ *Davis v. Bartlett*, 12 Ohio St. 534 (1861).

personally obligated unless the instrument names the person represented and shows that the signature is made in a representative capacity. And it adds that the name of an organization preceded or followed by the name and office of an authorized individual is a signature made in a representative capacity, thus settling the troublesome problem arising from an instrument signed, "The Smith Company, John Smith, President."

Under this section parol evidence is not admissible between the original parties to show that an instrument signed, "John Doe, Agent," and not containing the name of any principal, was not intended to bind John Doe individually. The corresponding section in the NIL is 20.⁶⁷ There is nothing in the Ohio law at odds with the proposed section.

Of course in this, as in other questions of parol evidence, the UCC is not intended to affect the admissibility of parol evidence in an action to reform the instrument.

Section 3-404. *Unauthorized Signatures*. Subsection 2 settles in the affirmative the question as to whether or not a forged signature may be ratified. Ohio has held that it may not, but has recognized that a person may be estopped to deny the validity of his signature.⁶⁸ The proposed change is only a step beyond the present law, and there seems to be no reason for opposing it.

Section 3-405. *Impostors: Signature in Name of Payee*. This section replaces Section 9(3) of the NIL⁶⁹ and includes both the so-called "fictitious payee" and "impostor payee" cases. The term "fictitious or nonexistent person," which appears in the NIL, is dropped as being misleading, and the paper is no longer designated as "bearer" paper, which, in truth, it is not, inasmuch as it is made out to a named payee.

The impostor payee situation is covered in Section 3-405(1)(a). Speaking generally there are two main types of impostor cases. The first is where the impostor, in a face-to-face meeting with the victim, induces the latter to issue the instrument, designating as payee the name falsely used by the impostor. The second is where the impostor makes use of the mails or some other form of communication. In either case, an indorsement by the impostor or his confederate in the name of the designated payee will be effective. The section properly rejects decisions distinguishing between the face-to-face and the mail transactions.⁷⁰

The "fictitious payee" situation is covered by Subsections 1(b) and 1(c). A typical case included in the first of these subsections

⁶⁷ OHIO GEN. CODE Sec. 8125.

⁶⁸ *Workman v. Wright*, 33 Ohio St. 405 (1878); *Shinew v. First Nat. Bank*, 84 Ohio St. 297, 95 N.E. 881 (1911).

⁶⁹ OHIO GEN. CODE Sec. 8114(3).

⁷⁰ See BRITTON Sec 151.

is the following. Smith, a corporate officer authorized to sign checks, makes out a company check payable to the order of Jones. The company is not indebted to Jones, and Smith, the villain in the piece, indorses the name of Jones and subsequently indorses his own name and gets the check cashed. Under the UCC provision, as well as under NIL 9(3), the indorsement is effective and passes title.

The second subsection changes the NIL for the better. If, in the above example, Smith was not the agent who signed checks but merely supplied the information to an innocent officer who signed, the NIL would relieve the company from liability, regarding the indorsement as a forgery. This results from the requirement in the NIL section that the "fact" (i.e. the fictitious name) must be known to the person making the instrument so payable. The NIL thus distinguishes between the two situations referred to above. Such a distinction is without merit.

Section 3-406. *Negligence Contributing to Alteration or Unauthorized Signature*. This is a new section although case law has dealt with the problems involved,—sometimes unsatisfactorily.

In essence the section precludes a person who, by his negligence, substantially contributes to a material alteration of the instrument or to the making of an unauthorized signature, from taking advantage of the alteration or lack of authority against a holder in due course or against a drawee or other payor who pays the instrument in good faith and in accordance with the reasonable commercial standards of the drawee's or payor's business.

A stock example of contributing to a material alteration arises where the drawer of a check negligently leaves spaces in the lines pertaining to the amount, thereby facilitating alteration by a swindler. Although in general the cases throw the loss on the negligent drawer as against the drawee bank, there is a conflict among the decisions in a suit by the holder in due course against the drawer.⁷¹ The UCC settles the conflict in an equitable manner by imposing liability on the drawer.

An example of negligence contributing to the making of an unauthorized signature is found in the case of a person who has a signature stamp for signing checks, and is negligent in looking after it with the result that the wrongdoer obtains it and uses it on a check. Another example is the negligent mailing of an instrument to a person having the same name as the payee.⁷²

⁷¹ BRITTON Sec. 282. Ohio has allowed recovery by the holder in due course against the drawer. *Second Nat. Bank v. Campbell*, 4 Ohio App. 158, 21 Ohio Cir. Ct. (N.S.) 305, 30 Ohio Cir. Ct. 270, *motion to certify overruled*, 60 Week. L. Bull. 40 (1915).

⁷² *The S. Weisberger Co. v. Barberton Savings Bank*, 84 Ohio St. 21, 95 N.E. 379 (1911).

Section 3-407. *Alteration*. Although this is a rather complicated section, it does not effect any substantial change except in two respects. In conjunction with Section 3-115, as stated in my discussion thereof, the present section permits recovery by a holder in due course of an incomplete instrument undelivered. The other principal change may perhaps be better described as a removal of uncertainty. Whereas NIL Section 124,⁷³ interpreted literally, avoids a materially altered instrument as against a non-assenting party unless it is in the hands of a holder in due course, the UCC limits the discharge to an alteration by the holder which is both fraudulent and material. Consequently, neither a non-fraudulent alteration nor an alteration by a stranger will avoid the instrument. This is in conformity with Ohio authorities.⁷⁴

Section 3-408. *Consideration*. The most important feature of this section is found in the provision that no consideration is necessary for an instrument or obligation thereon given in payment of or as security for an antecedent obligation of any kind. As stated in the Comment on the section: "The provision is intended to change the result of decisions holding that where no extension of time or other concession is given by the creditor the new obligation fails for lack of legal consideration. It is intended also to mean that an instrument given for more or less than the amount of a liquidated obligation does not fail by reason of the common law rule that an obligation for a lesser liquidated amount cannot be consideration for the surrender of a greater."

Section 3-410. *Definition and Operation of Acceptance*. Obsolete forms of acceptance, recognized in the NIL, are eliminated. These include acceptance for honor, and virtual and collateral acceptances.⁷⁵ Section 137 of the NIL⁷⁶ is likewise eliminated. It provides for constructive acceptance by delay or refusal to return the instrument or destruction thereof, and has caused endless confusion.⁷⁷ The UCC treats the problem under Section 3-419, dealing with conversion. I will refer to the matter again in discussing that section.

Section 3-411. *Certification of a Check*. Subsection (1) continues the distinction whereby the drawer and all prior indorsers are discharged if the holder procures certification, whereas a certification procured by the drawer leaves him liable.⁷⁸

Subsection (2), which is new, codifies the existing case law

⁷³ OHIO GEN. CODE Sec. 8229.

⁷⁴ 29 OHIO JUR., *Negotiable Instruments* Secs. 325, 327.

⁷⁵ NIL Secs. 161-170, 134, 135; OHIO GEN. CODE Secs. 8266-8275, 8239, 8240.

⁷⁶ OHIO GEN. CODE Sec. 8242.

⁷⁷ BRITTON Sec 179.

⁷⁸ NIL Sec. 188; OHIO GEN. CODE Sec. 8293; BRITTON Sec. 180.

in providing that unless otherwise agreed, a bank has no obligation to certify a check.⁷⁹

Subsection (3), also new, recognizes the practice of certifying a check before returning it for lack of proper indorsement. Such action discharges the drawer.

Section 3-412. *Acceptance Varying Draft*. The qualified acceptance, a remnant of the horse and buggy era, is eliminated. If the drawer's proffered acceptance varies the draft, the holder may refuse it and treat the draft as dishonored. If, on the other hand, the holder assents to the acceptance, each drawer and indorser who does not affirmatively assent is discharged except where the variance is that payment shall be made only at a particular place. Moreover, the terms of the draft are not deemed to be varied by an acceptance to pay at any bank in the United States.

Section 3-413. *Contract of Maker, Drawer and Acceptor*. Section 62 of the NIL⁸⁰ has caused difficulty in the case of an instrument altered and subsequently accepted. I will give an example in order to illustrate the problem. Under Section 62 the acceptor agrees to pay the instrument according to the tenor of his acceptance and he admits certain things such as the genuineness of the drawer's signature. The correctness of the amount appearing on the instrument is not listed among the admissions. Does that mean that if the amount has been fraudulently raised, the acceptor is liable only for the original amount? Or does his agreement to pay according to the tenor of his acceptance make him in effect a guarantor of the amount shown at the time of his acceptance? Or does "tenor of acceptance" relate merely to the nature of the acceptance, i.e., whether general or qualified?⁸¹ Solving the riddle the UCC makes it clear that his engagement to pay relates to the tenor of the instrument at the time of the engagement. The section applies to all drafts, including checks.

Section 3-414. *Contract of Indorsers: Order of Liability*. Section 66 of the NIL⁸² embraces the indorser's liability as such and his liability on the warranties of a transferor. The UCC separates them, and the present section deals with the first-named liability. It should be especially noted that the indorser engages to pay the instrument according to its tenor at the time of his endorsement. Thus, if the instrument has previously been altered, his engagement is to pay it as altered.

Subsection (2), dealing with order of liability among indorsers,

⁷⁹ E.g., *Wachtel v. Rosen*, 249 N.Y. 386, 164 N.E. 326, 62 A.L.R. 374 (1928).

⁸⁰ OHIO GEN. CODE Sec. 8167.

⁸¹ See BRANNAN, *NEGOTIABLE INSTRUMENTS LAW* 904, 917-919, 920-923 (7th ed., Beutel, 1948).

⁸² OHIO GEN. CODE Sec. 8171.

makes no change and is intended merely to clarify existing law under NIL Section 68.⁸³

Section 3-415. *Contract of Accommodation Party*. With regard to accommodation parties the UCC is a big improvement over the NIL. It combines three sections into one, clarifies the wording, and adds new matter.

The section specifically recognizes that an accommodation party is a surety regardless of the capacity in which he signs. Moreover, the words "without receiving value therefor," found in NIL Section 29,⁸⁴ have been eliminated. Those words have given rise to the question whether a paid surety may be an accommodation party. The UCC clearly answers the question in the affirmative.

Subsection (4) introduces a new and logical provision that an indorsement which shows that it is not in the chain of title is notice of its accommodation character.

Under the NIL courts have held that an accommodation party who signs after the instrument is in the hands of a holder who has given value, is not liable in the absence of some new consideration.⁸⁵ Subsection (2) of the UCC section under discussion is designed to change such a rule.

Subsection (5) makes it clear, contrary to some authority, although not the majority,⁸⁶ that an accommodation party who pays the instrument has a right of recourse *on the instrument* against the party accommodated.

Section 3-416. *Contract of Guarantor*. The NIL does not tell us the effect of words of guaranty added to a signature. Consequently, courts have had trouble in fitting such words into the law of negotiable instruments.⁸⁷ The UCC comes to the rescue by setting forth the meaning of "Payment guaranteed" and "Collection guaranteed," or equivalent words. When words of guaranty are used, presentment, notice of dishonor, and protest are not necessary to charge the user. No change is effected in Ohio law.

Section 3-417. *Warranties on Presentment and Transfer*. Under NIL Sections 65 and 66,⁸⁸ there is no warranty in favor of the person paying or accepting the instrument. Instead, the warranties are limited to transferees. Thus payors and acceptors are ordinarily dependent upon quasi-contractual doctrines pertaining to money paid or promised under mutual mistake of fact. The UCC extends the warranty benefits to payors and acceptors.

Subsection (1) (c) settles a problem which is not clear under

⁸³ OHIO GEN. CODE Sec. 8173.

⁸⁴ OHIO GEN. CODE Sec. 8134.

⁸⁵ BRITTON Sec. 94.

⁸⁶ BRITTON Sec. 297.

⁸⁷ See BRITTON Sec. 59.

⁸⁸ OHIO GEN. CODE Secs. 8170, 8171.

the NIL. The problem arises from the payment or acceptance of a draft or check which has been materially altered. The UCC follows the common law rule permitting the good faith payor to recover and the good faith acceptor to avoid his acceptance. An exception is made, as it should be, where the drawee bank accepts an already altered draft which subsequently reaches a holder in due course.⁸⁹ An exception is made also in the case of a holder in due course of a note. In neither of these instances does the holder in due course warrant against alteration.

Subsection (2) clarifies some difficult conflicts arising from the rather vague language of NIL Sections 65 and 66. By Subsection (2) (d) it is made clear that the transferor, without indorsement, warrants to his immediate transferee that no defense of any party is good against him and that the general indorser warrants the same thing to any subsequent good faith holder. However, this warranty is not applicable to an indorser without recourse, who, by Subsection (3), warrants merely that he has no knowledge of such a defense.

By Subsection (2) (e), relating to the insolvency of the maker, acceptor, or drawer of an unaccepted draft, it is made clear that there is no warranty against insolvency as such. Rather, the transferor warrants that he has no knowledge of the institution of any insolvency proceeding.

Section 3-418. *Finality of Payment or Acceptance.* The famous English case of *Price v. Neal*⁹⁰ held that a drawee who accepts or pays a draft on which the drawer's signature is forged, is bound on his acceptance and cannot recover back his payment. Section 62 of the NIL⁹¹ covers the acceptance situation but is silent with reference to payment. Most courts have followed the common law rule with reference to payment, some stating that NIL Section 62 was meant to include payment.⁹² The UCC makes it clear that such a payment or acceptance is final in favor of a holder in due course. In this latter respect the UCC goes further than some decisions which, by way of modification of the rule, permit recovery by the payor on the basis of mere negligence on the part of the holder in taking the instrument.⁹³ Under the UCC rule a holder in due course would win, even though negligent.

The present section must be read in conjunction with Section 3-417, dealing with warranties.

Section 3-419. *Conversion of Instrument; Innocent Represent-*

⁸⁹ See the discussion in connection with Section 3-413, *supra*.

⁹⁰ 3 Burr. 1354, 97 Eng. Rep. 871 (K.B. 1762).

⁹¹ OHIO GEN. CODE Sec. 8167.

⁹² BRITTON Sec. 135.

⁹³ BRITTON Sec. 136.

ative. Sections 136 and 137 of the NIL⁹⁴ have caused a great deal of difficulty and conflict. They deal with the retention and destruction of drafts presented for acceptance, and give rise to the so-called constructive acceptance. Moreover, courts have extended them so as to include checks presented for payment.⁹⁵ As we have already noted, UCC Section 3-410 has abolished this form of acceptance. The present section recognizes that refusal to return the instrument on demand is a conversion, giving rise to an action in tort rather than on the draft or check.

Another problem settled by this section arises from the following typical facts. A person steals a check from the payee, forges the payee's name as indorser, and gets the check cashed. The drawee innocently pays the check. The payee, who is the true owner, sues the drawee for the amount of the check. Most courts hold that there is no recovery on the basis of acceptance, since payment to the wrong party is not a promise to pay the owner.⁹⁶ However, recovery against the drawee has been upheld on the basis of conversion.⁹⁷ Subsections (1) (c) and (2) recognize this principle and designate the face amount of the instrument as the measure of damages.

PART V.

PRESENTMENT, NOTICE OF DISHONOR, AND PROTEST.

Sections 3-501 through 3-511 relate to presentment, notice of dishonor, and protest. Nearly one-third of the NIL is concerned with these topics, whereas the UCC covers them in eleven sections. The reduction is accomplished by elimination, simplification, and reorganization. There is no point in laboring through the whole business. In general, the requirements are similar to those of the NIL. Consequently, it is enough to point out some of the more significant changes and developments.

Section 3-501, stating when presentment, notice of dishonor, and protest are necessary, contains two important changes. Under Section 70 of the NIL,⁹⁸ drawers of drafts other than checks are wholly discharged by a failure to make due presentment, but drawers of checks are, by that section, in conjunction with Section 136,⁹⁹ discharged only to the extent of the loss caused by the delay. Such a loss arises from the insolvency of the drawee bank, occurring after the time when presentment was due. Subsection (1) (c)

⁹⁴ OHIO GEN. CODE Secs. 8241, 8242.

⁹⁵ BRITTON Sec. 179.

⁹⁶ BRITTON Sec. 146; *Elyria Savings & Banking Co. v. Walker Bin Co.*,

92 Ohio St. 406, 111 N.E. 147 (1915).

⁹⁷ BRITTON Sec. 146.

⁹⁸ OHIO GEN. CODE Sec. 8175.

⁹⁹ OHIO GEN. CODE Sec. 8291.

changes the NIL by putting drawers of drafts in the same situation as drawers of checks. That situation is described in Section 3-502 (1) (b), *infra*. The acceptor of a draft payable at a bank and the maker of a note payable at a bank are placed in the same category.

Another important change in the present section relates to protest. Under Subsection (3) protest is necessary only in the case of a draft which on its face appears to be drawn or payable outside of the states and territories of the United States and the District of Columbia. Under NIL Sections 129 and 152, combined,¹⁰⁰ protest is required not only in the above situations, but even in the case of a bill appearing on its face to have been drawn in one state and payable in another. The inconvenience and expense of protest justifies the change effected by the UCC.

Section 3-502. *Unexcused Delay: Discharge*. As indicated in my remarks concerning the previous section, the present section tells what happens in the case of an unexcused delay in presentment or notice of dishonor. There is no need to repeat which parties are not wholly discharged. An example will point up the problem. The holder of a check delays unduly in presenting it for payment. The drawee bank fails. Under NIL Sections 70 and 186,¹⁰¹ the drawer is discharged to the extent of the loss caused by the delay. But how may the loss be ascertained? The liquidation of the bank is likely to take years, and until it is concluded, the extent of the drawer's loss may be unknown. Without changing the principle of the NIL, the present section of the UCC solves the difficulty in a practical and fair manner. Subsection (1) (b) permits the drawer to discharge his liability on the instrument by a written assignment to the holder of the drawer's rights against the drawee bank with respect to his funds in the bank, and provides that he is not otherwise discharged.

Section 3-503. *Time of Presentment*. The most important variation in this section from the corresponding NIL provisions concerns the question of reasonable time in the presentment of uncertified checks for payment. We have seen that if a check is presented too late, the drawer is discharged under NIL Section 186¹⁰² to the extent of the loss caused by the delay, and that the UCC Section 3-502 contains a comparable provision. But what is a reasonable time? Lawyers and courts have struggled with the problem. Subsection (2) of the present UCC section gives us a yardstick by providing that with respect to the drawer, thirty days shall be presumed to be a reasonable period within which to present for

¹⁰⁰ OHIO GEN. CODE SECS. 8234, 8257.

¹⁰¹ OHIO GEN. CODE SECS. 8175, 8291.

¹⁰² OHIO GEN. CODE SEC. 8291.

payment or initiate bank collection. In the case of an indorser, who is wholly discharged by a delayed presentment, the presumption is seven days after his indorsement.

In passing, it is of interest to note that many courts have adopted a one-day rule for presentment.¹⁰³ Such a short period is unrealistic, and the UCC presumption is more sensible and just. Even the courts which have the one-day rule often stretch it by exceptions. Some Ohio cases have employed the one-day rule,¹⁰⁴ but there is no apparent policy preventing the UCC improvement.

Section 3-510. *Evidence of Dishonor and Notice of Dishonor.* This is a new section, which, as the title indicates, specifies items which are admissible as evidence and create a presumption of dishonor and notice of dishonor. There is nothing revolutionary about the section. It merely aids in the proof of these matters by the adoption of common sense rules of evidence and presumption.

PART VI.

DISCHARGE.

Sections 3-601 — 3-606, relating to discharge, create few important changes in the existing law. However, they reorganize the subject matter in a manner more clear and concise than that employed in the NIL.

The concept of the discharge of the instrument is abandoned;¹⁰⁵ in its place is substituted the more accurate concept of the discharge of parties.

Section 3-602 removes an uncertainty not settled in the NIL, by providing: "No discharge of any party provided by this Article is effective against a subsequent holder in due course unless he has notice thereof when he takes the instrument." Thus, for example, if the maker pays the instrument before due, and does not obtain it from the person to whom he makes payment, the defense is cut off when the instrument reaches a holder in due course.

Section 3-603 (1) is similar to NIL Section 88,¹⁰⁶ but more securely protects the rights of a person paying the instrument in the face of a claim to the instrument by another person. The NIL section protects the payor if he pays the holder in good faith and without notice that his title is defective. The UCC gives the payor more definite protection by authorizing the payment even though he has knowledge of the third person's claim unless prior to the payment the claimant either supplies adequate indemnity or enjoins payment by court order. As stated in the Comment: "There is no good reason to put him [the payor] to inconvenience because

¹⁰³ BRANNAN, *NEGOTIABLE INSTRUMENTS LAW* 1296 (7th ed., Beutel, 1948).

¹⁰⁴ E.g., *Davis v. Benton*, 2 Ohio Dec. Rep. 329 (Com Pl. 1860).

¹⁰⁵ NIL Sec. 119, OHIO GEN. CODE Sec. 8224.

¹⁰⁶ OHIO GEN. CODE Sec. 8193.

of a dispute between two other parties unless he is indemnified or served with appropriate process." After all, his contract is to pay the holder.

Section 3-604. *Tender of Payment*. There is one change in the law in this section. Section 70 of the NIL¹⁰⁷ has been taken to mean that makers and acceptors of notes and drafts payable at a bank are not discharged to any extent by failure of a holder to make due presentment at the bank. That is because, technically, they are primary parties.¹⁰⁸ The UCC reverses the rule and, as in other sections, places instruments payable at a bank in their proper setting.

Section 3-606. *Impairment of Recourse or of Collateral*. This section solves satisfactorily a problem not directly covered by the NIL and giving rise to conflict in the decisions. Section 120 of the NIL,¹⁰⁹ relating to the discharge of persons secondarily liable, includes discharge by an agreement to extend the time of payment, made without the assent of the secondary party. Unfortunately, Section 119,¹¹⁰ concerning discharge of "the instrument," does not contain a similar term. As a result, the following inequitable situation arises. Smith and Jones are co-makers of a negotiable promissory note. Smith is the principal obligor, and Jones is a surety. Without the assent or knowledge of Jones, Smith and the holder agree to extend the time of payment. Since Jones is not a secondary party, he does not have the benefit of Section 120 and therefore remains liable.¹¹¹ Yet by common law principles of suretyship, he would be discharged. Section 3-606 remedies the defect by broadening the discharge to cover any party. In addition, the section discharges a party in case of the holder's unjustifiable impairment of collateral given by the party or by a person against whom he has a right of recourse. This fills another gap in the NIL. The Ohio Supreme Court reached this palpably desirable result despite the NIL.¹¹²

PART VII.

COLLECTION OF DOCUMENTARY DRAFTS.

Sections 3-701 through 3-704, relating to the collection of documentary drafts, are almost entirely new but do not appear to be controversial. They state in some detail the rights and duties of a bank handling a documentary draft for a customer. A documentary

¹⁰⁷ OHIO GEN. CODE Sec. 8175.

¹⁰⁸ BRITTON Sec. 973.

¹⁰⁹ OHIO GEN. CODE Sec. 8225.

¹¹⁰ OHIO GEN. CODE Sec. 8224.

¹¹¹ Richards v. Market Exchange Bank, 81 Ohio St. 348, 90 N.E. 1000 (1910).

¹¹² Goodman v. Goodman, 127 Ohio St. 223, 187 N.E. 777 (1933).

draft is defined in Section 4-104 as "any draft with accompanying documents, securities or other papers to be delivered against honor of the draft."

PART VIII.

MISCELLANEOUS.

Section 3-802 (3) stipulates that where a check or "similar payment instrument" provides that it is in full satisfaction of an obligation, the payee discharges the underlying obligation by obtaining payment of the instrument unless the original obligor has taken unconscionable advantage. Contrary to the law in some states,¹¹³ this provision permits an accord and satisfaction even where the obligation is for an undisputed and liquidated debt. A number of examples in the Comment illustrate situations in which the payee is protected by reason of an unconscionable advantage taken by the obligor. With this protection, the rule enunciated by the subsection is a healthy advance in the law of accord and satisfaction.

Section 3-803 is new and is designed to prevent multiplicity of suits. It provides that in an action on an instrument a defendant may give written notice to any third person who is or may be liable on the instrument, advising such person of his right to intervene and that he will be concluded by any decision rendered. The person notified may give similar notice to others. Any person so notified may intervene, but even if he does not do so, he is concluded as to any issue of fact therein determined.

Section 3-805 serves the excellent purpose of subjecting to Article 3 instruments otherwise negotiable but not made payable to order or bearer. The section includes the provision that there can be no holder in due course of such an instrument. These non-negotiable instruments have been stepchildren of the law, and the decisions concerning them are in conflict. The present section resolves the conflict in a businesslike manner by giving them all the advantages of commercial paper except those accruing to a holder in due course.

CONCLUSION.

In this article I have considered a number of individual sections of the proposed UCC and have endeavored to point out their relationship to the NIL and their improvement over the NIL. As stated at the outset, it has not been my purpose to discuss the problems as fully as might be wished, for limitations of time and space have necessitated comparatively abrupt treatment. Moreover, the main function of this article is not to lead the reader into lengthy arguments and explanations, but rather to cover a good

¹¹³ 1 C. J. SEC., *Accord and Satisfaction* Secs. 31, 35 (1936).

deal of ground, albeit in a cursory manner, in order that he may understand what the UCC will do in a large number of specific situations.

Disagreement in detail is bound to accompany consideration of a proposed code of the scope of the UCC. But it should be remembered that this Code is the product of years of labor by lawyers, judges, and law teachers, who have gone through it with a fine-tooth comb. Certainly so far as Article 3 is concerned, it is my opinion that the Code is a vast improvement over the NIL and should be adopted in Ohio.